

Meeting Date: 12-09-08

AGENDA REPORT

City of Santa Clara, California

Agenda Item #

7C-2



Date: December 9, 2008

To: City Manager for Council Information

From: Mary Ann Parrot, Director of Finance
John Roukema, Electric Utility Director
Alan Kurotori, Water and Sewer Utility Director

Subject: Impact of Financial Crisis on City of Santa Clara

EXECUTIVE SUMMARY

This memo was discussed at the December 2 City Council meeting; no action is needed. The following information will summarize the impact of the recent financial crisis on City finances through October 2008. The key revenue streams involved to date are as follows:

- General Fund: Sales tax revenues, Transient Occupancy Tax (TOT) revenues, Property Tax revenues
- Redevelopment Agency (RDA) and Tax Increment Revenues: State budget impact and impact of assessed value declines on 2011-12 property tax revenues
- Enterprise Funds: Electric Utility and Water & Sewer Utility
- Other funds: Investment earnings and pension costs are also addressed

Because of the newness of the crisis, as well as the staggering proportions of its impact, it is not possible at this time to predict the final outcome of the recession on the City's finances. In order to quantify the impact of this crisis on the City's finances, more information will be needed in the next several months. City Council receives a mid-year report during the annual budget cycle, in February for the period covering July-December of the current fiscal year. Staff will have more information about the factors in flux at that time, and will be better able to determine the impact of the most recent two months (September and October) of the on-going financial crisis affecting the country and the region at that time.

General Fund

Sales Taxes

Sales Tax revenues comprise 27% of the City's General Fund. In the case of Sales Tax Revenues, revenues for the 1st and 2nd quarters of 2008 were down.

- Most cities' sales tax collections in Santa Clara County are down for the past two quarters. The information for July-September, 2008 will be available in January, 2009.
- All sectors in the City of Santa Clara are down for the 2nd quarter calendar year except for one sector, as follows:
 - Total receipts are down by 6.9%
 - General retail is down by 7.9%
 - Business to business is down by 5.5%
 - Transportation (autos, new and used, service stations) is down by 13.3%, most of this due to significant declines in auto sales
 - Miscellaneous (health care, other) is down 20.7%

- Construction, wholesale and retail, is down 0.3%
- Food products was up 0.6%

If the downward trend persists, the City will realize a decline in revenues for the year of \$2 million to \$3 million.

Transient Occupancy Taxes (TOT)

TOT comprises 7.9% of the City's General Fund. With regard to TOT, for four months of this year through October 31, 2008, revenues were ahead of last year's figures for the same period of time by 2.8%. From a budget perspective, the City had collected 39.7% of budgeted amounts, which is slightly ahead of projections. Without having additional information, the conclusion would be that the City would expect to collect budgeted amounts of \$11.8 million. Therefore, it remains to be seen whether the current pace of collections will continue, and Staff will have more information after the first of the year.

Property Taxes

Property Taxes comprise 19% of the City's General Fund. This is budgeted at \$28.6 million for 2008-09. Collections to date lag what is expected, primarily due to the fact that most of the receipts are reported later in the year. In a meeting with County officials in mid-November, the report released by the County showed a decline of \$200,000 in property tax collections for the City of Santa Clara. This covers the non-RDA and RDA collections, and secured and unsecured (business personal property) collections. It excludes the \$2.022 million take-away required by the State Budget, which is also covered under the section below titled Redevelopment Agency (RDA). Staff receives a monthly report from the County and will follow closely the variables involved in determining the final outcome: assessed valuations, appeal processing and corrections performed by the County, refunds, etc.

Redevelopment Agency (RDA)

The most significant impact of the State Budget actions is relevant to the Redevelopment Agency (RDA) for 2008-09 appropriated funds: \$2,022,178 million must be paid to the State by May10, 2009, from RDA funding for the fiscal year 08-09, as detailed in AB1389, the trailer bill to the state budget legislation. Additional information is presented on this item below.

- This is a one-time take-away, not to be repaid by the State. It is also not a loan to be repaid by the State. The \$2.022 million represents the City's RDA share of a take-away of \$350 million statewide.
- The Governor's November call for an additional special legislative session included the possibility of a permanent, annual take-away of \$400 million, which would translate into a permanent take-away of over \$2 million for the City's Redevelopment Agency. Staff will apprise City Council of additional information as the discussions develop at the State level.
- Declines in assessed valuation of properties in the RDA areas could lead to less tax increment in 2011-12, when the declines over this year and next in the secured and unsecured rolls are realized on the tax rolls. Staff continues to monitor this on a monthly basis.

Enterprise Funds (Electric Utility and Water and Sewer Fund)

Electric Utility

For the period through October 31, 2008, electric utility revenues for customer charges stood at 34% of budget, slightly above the expected level of 33% for four months, notwithstanding seasonal variations in loads, etc. For the same period last year, the level was 30% of budget, below the expected level of 33%.

Impact on interest rates and interest expenses for Electric Utility variable rate bonds

During 2008 the City issued the 2008A variable bonds to replace the 2003B auction rate bonds, and the 2008B variable rate bonds (in conjunction with a 2006 JPMorgan swap) to replace the 1998A fixed rate bonds. Even though variable interest rates have been elevated at times, through October of the current fiscal year, costs for the 2008A and 2008B variable rate bonds/JPMorgan swap, are approximately equal to budgeted amounts.

Impact of dry hydroelectric conditions on production costs

Unrelated to the financial crisis, continuing dry hydroelectric conditions have caused production costs to be higher than budgeted. Through October, this impact is estimated to be approximately \$10 million. All other things being equal, this will ultimately cause an additional drawdown in the Cost Reduction Fund.

Staff continues to evaluate the capital and operating needs of the enterprise and will return to City Council in the first quarter, 2009, with additional information.

Water and Sewer Fund

The first quarter of the fiscal year water sales and sewer use are 5% lower than the same period in Fiscal Year FY 07/08. The water and sewer utility revenues are at 37% for the first four months of the fiscal year, which is below the previous year revenues for the same period of 38% and 40% in FY07/08 and FY06/07 respectively.

The sewer utility system is planning for significant capital improvements necessary over the next several years including the sanitary sewer conveyance system improvements, and the City's share of necessary capital improvements at the San Jose/Santa Clara Water Pollution Control Plant.

The Public Works Department completed a sanitary sewer capacity assessment study (study) in 2007-08, which forecasted the need to increase the sewer conveyance capacity based on the current 2010 General Plan. The study concluded with the need for approximately \$25 million in capital improvement projects costs necessary in the next 2-3 years. Staff has proposed in the 2008-09 adopted budget to issue bonds for this project, as it is sizeable and funds are not on hand to finance these large CIP projects. The utility does not have cash on hand for this large a capital project. In anticipation of these projects, City Council approved the Sewer Conveyance Fee to charge to developers for connection to the system. However, the Sewer Conveyance Fee will not be adequate to pay for the up front project costs, especially since the downturn in the economy and expected long-term recovery. The Sewer Utility is finalizing a rate study to present to City Council later in the fiscal year. Over the past several years, the Sewer Utility has been able to rely on modest rate increases, and the prudent use of reserves to hold down rates over the past few years. However, the use of \$1 million in reserves this year will deplete the reserve position of the utility to a level which will make it difficult to issue bonds. In addition, the current revenues will not provide the coverage necessary for the bond debt service. Staff will return to City Council in the next few months to review their recommendations for sewer rates going forward.

The Sewer Utility will also need to budget for the significant long-term capital projects at the San Jose/Santa Clara Water Pollution Control Plant (Plant) over the next several years. An early estimate is \$1 billion in capital improvements are necessary for aging infrastructure and deferred maintenance. The Plant has

initiated a multi-year Plant Master Plan to guide cost effective reinvestment in the plant infrastructure, and maximize the beneficial use of the treatment plant lands. Additional information will be presented to City Council as it is available.


Other City Funds

Investment Policy and Investment Portfolio

The City has an approved Investment Policy and meets quarterly to review the portfolio holdings. The City uses an investment strategy titled "buy and hold" which means the City buys high quality bond investments and holds them to maturity. In this way, the City does not experience capital gains or losses on specific investments. The City also does not have any holdings in the companies announcing bankruptcy in the past several months. The interest earnings on the bonds continue to flow in to the City accounts.

Impact on City Pension Investments at California Public Employee Retirement System (CalPERS)

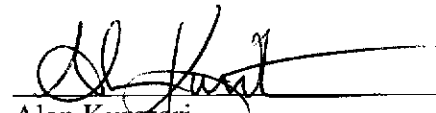
CalPERS has announced a decline in value of 5.1% for the year 2007-08 and over 20% year to date. If this persists for the entire year, the City will see rate increases of 2% to 5% in 2011-12.



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APPROVED:



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